Comments on the House Agriculture Committee Farm Bill Proposal

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On behalf of the
Coalition for a Competitive Food and Agricultural System

House Agriculture Committee
July 19, 2001

Good morning. I am Bruce Ritter, Executive Vice President of the Louis Dreyfus Corporation, a worldwide merchant and trader of agricultural commodities as well as a provider of financial risk management services to other agri-businesses. I also own and help my brother manage our family's farm in Oregon where we grow cattle, alfalfa, and small grains.

I am representing the Coalition for a Competitive Food and Agricultural System (CCFAS). Louis Dreyfus is one of about 120 agri-business companies and agriculture related trade associations, which make up the membership of CCFAS; a coalition committed to market-oriented policies and programs for US agriculture.

Agri-business representatives like myself are sometimes thought to be suspect when commenting on farm programs. How many times have we all heard that agri-business companies want farm programs and policies that will tend to keep farm commodity prices low? I assure you that CCFAS is not advocating a policy of low commodity prices. Growers and agribusinesses both do well when there is strong demand for agricultural products. The farm policy desires of growers and CCFAS are identical – a policy which will help foster growth and opportunity for US agriculture.

When the Congress approved "Freedom to Farm" Legislation in 1996, some in the agricultural community believed prices would remain strong forever due to strong international demand. Now some have become disenchanted with international trade and some even blame "Freedom to Farm" legislation for low prices over the last few years. This is shortsighted. The reason strong prices didn't last is because strong prices always set into motion the supply demand adjustments which will eventually bring on a period of lower prices.

The low prices of the last several years have also set motion the adjustments - greater consumption and a smaller land area planted to the major crops - which will bring world commodity prices to higher levels.

In the last three years, world consumption has exceeded production, even though the world has experienced three years of generally good weather and good crop production.

Stocks in China, Russia, other countries of the Former Soviet Union (FSU), and India have been significantly reduced. In China alone, grain stocks have been drawn down by tens of millions tons.

Today is not the time for the Congress to be inward looking on agricultural trade and approve a farm bill that reverses the reforms of “Freedom to Farm” legislation. US export competitiveness starts with market oriented farm programs. There is strong world demand and therefore good opportunities for US export growth over the next several years.

So what does CCFAS think of the House Agriculture Committee farm bill proposal? The proposal includes some of the major reforms of the 1996 Agriculture Market Transition Act, (AMTA) often referred to as "Freedom to Farm". CCFAS supports the following elements of the proposal:

- Planting flexibility, which allows growers to respond to market price signals without the threat of losing government farm program benefits.
- Continuation of a marketing loan program which will allow prices to move below the loan rate and keep US commodities competitively priced in world markets.
- No farmer owned reserve or similar government supply control program, which would cause stocks to build and depress commodity prices.
- Continuation of fixed direct payments for growers, which are decoupled from production.
- Addition of a new fixed direct payment program for soybeans combined with a reduction in the soybean loan rate.

Unfortunately, this proposal also takes US farm programs "Back to the Future" by re-creating the "target price" concept. CCFAS is opposed to the following elements of the proposal:

- Target price program.
- Rigid loan rates, which are unconnected to market prices.
- The option for the grower to update payment acreages.
- The increase in the authorization of Conservation Reserve Program from 36.4 million acres to 40 millions acres.

Target Price Program

A target price payment program, which is counter-cyclical to changes in commodity prices, will be market and trade distorting. Growers will know they will be protected by target price payments if excessive production occurs - the more excessive the production - the more they are protected.

Growers need a safety net, which will provide a cushion from lower commodity prices and lower incomes. Growers do not need a safety blanket that insulates them from necessary adjustments to market conditions. This target price proposal is not a safety net, but more like a blanket, which could further slow needed market adjustments and push US agriculture into longer periods of low prices.

Furthermore, when the US government steps in to eliminate too much risk for growers, the opportunities for stronger prices may also be limited.

Government support for Major Crops
Crop Year 2002

Crops	Current Law					Proposed
	$/Unit	Loan Rate *(expected loan rate)1*	AMTA *(Direct Payment)*	Market Loss *(Payments) 2*	Total	Target Price
Wheat	Bu.	$2.58	$0.46	$0.46	$3.50	$4.00
Corn	Bu.	$1.89	$0.26	$0.26	$2.41	$2.75
Cotton	Lb.	$.5198	$.0554	$.0554	$.5752	$.729
Rice	Cwt.	$6.50	$2.04	$2.04	$8.54	$10.71
Soybeans	Bu.	$5.26		$0.18	$5.46	$5.76

Assumptions:
[1] The Secretary of Agriculture would use discretion to freeze loan rates at current levels.
[2] Congress would continue market loss payments based on doubling of 2002 AMTA payments.

Compared to current law, this proposal for crop year 2002 would increase support from about $3.50 per bushel for wheat to $4.00 per bushel, from about $2.40 per bushel for corn to $2.75 per bushel, from about $.575 per pound for cotton to $.729 per pound, from about $8.50 cwt for rice to $10.71 cwt, and from about $5.50 per bushel for soybeans to $5.76 per bushel, respectively.

However, this increased support for growers is not assured. If market prices are higher than the target price, growers will not receive payments, or even worse, will need to re-pay advanced deficiency payments.

Grower Income Uncertainty

Most growers, and especially their lenders, like the predictability and certainty of fixed direct payments. No one is expecting commodity prices to reach target price levels anytime soon, but as growers learned in the mid 1990s, rising commodity prices in some years will reduce or even eliminate target price program payments.

Budget Uncertainty

The certainty and predictability of farm program costs is an advantage of fixed direct payments. The Congressional Budget Office (CBO) budget baseline assumes a price forecast where prices move steadily higher through the life of the next farm bill. It is of course, impossible to forecast prices for a 5-6 year period. There are just too many variables that could affect commodity prices such as weather problems in numerous producing and consuming countries, the changing value of the dollar relative to other currencies and stronger world demand from rising incomes, improved market access for US commodities and many other factors.

Season Average Price Projections
Congressional Budget Office (CBO)

Back Door Toward Acreage Reduction Programs

If the Congress approves and the President signs into law a farm bill with a target price program, large unexpected program spending could force the Congress to eventually change the program.

Without changing the formula for determining target price payments, there are only two ways to try to control spending.

- Reduce the payment acreage on which payments are made from 85 percent to a lower number.
- Impose Acreage Reduction Programs (ARPs) that jeopardize the international competitiveness of US agriculture.

World Trade Organization (WTO) Limits on Agriculture Subsidies

Target price payments are "amber box" WTO trade distorting subsidies and will count toward limits agreed to by the United States in the Uruguay Trade Agreement. But more important than current WTO trade limitations, is the need for the United States to further liberalize trade in agricultural products in a new round of multilateral trade talks scheduled to begin in Qatar in November.

Trade liberalization is the engine of world economic growth. Export demand for US agricultural products will only improve through world income growth and improved market access obtained in trade negotiations. Since 96% of the world population lives outside the United States, the only significant opportunity for growth in US agriculture is from growth in international trade.

Adoption of an additional trade distorting "amber box" farm program would be a relinquishing of the US leadership position on liberalizing trade in agricultural products. If the US does not lead on trade, one of two things will happen. The US will be left behind in negotiations and placed at a disadvantage to other trading partners or, more likely, very limited progress will be made in improving the world-trading situation in agricultural products. Other countries will follow the lead of the United States and seek to preserve or expand domestic subsidies, rather than reach for the potential for increased trade.

To trade potential progress on world trade liberalization for a few billion dollars in "amber box" farm program payments – when the US could set the world example and make the payments in non-trade distorting direct payments is a very poor trade-off for all of US agriculture.

Effect of the Proposal on Land Values

Government payments, even direct de-coupled payments are capitalized into land values.

Growers are always trying to lower costs by spreading fixed labor and equipment over more cropland. In competition with other growers, the government payment is very quickly bid into the price of land or land rent.

USDA in a recent study concluded that about 25 percent of US cropland value was due to government payments. Because of large government payments, national cropland values have continued to rise even while market returns have declined during the last 3-4 years.

This proposal is likely to add to this trend of higher land values which some have characterized as a government induced farmland price bubble.

In the long term, this government fueled land price trend puts US growers in a classic cost-price squeeze. Land is the single largest cost of production and US growers will be unable to compete with growers in the rest of the world without continually rising farm program payments. Farm program spending surely will not be able to increase indefinitely because there are too many other federal budget needs – education, prescription drug benefits for senior citizens, social security reform, military preparedness, etc.

A farm asset devaluation sometime in the future is a possibility unless world commodity markets strengthen and provide higher market returns.

Rigid Loan Rates

Although a slightly lesser concern of CCFAS, rigid loan rates also can become an incentive for growers to plant for the commodity loan program. Although some members of CCFAS disagree, I believe that the oilseed loan rates in recent years have been at levels, which caused growers to increase oilseed planted acreage to the detriment of planted acreage of other crops.

CCFAS believes loan rates should be linked to market prices and be adjusted each year. Otherwise, loan rates can become out of line with market prices.

Producer Option to Adjust Payment Acreage

CCFAS is concerned about the proposal to allow updating of payment acreage because it jeopardizes the "green box" classification of direct payments. Will growers be allowed to update payment acreage at the expiration of each farm bill?

It is critical that Congress level farm program benefits for all commodities. Otherwise planted acreage will shift toward the commodity with the most lucrative government benefits and growers will want to update payment acreage to continue receiving the more lucrative government benefit in future years. CCFAS also questions whether this potential shift in payment acreage has been considered in the budget analysis?

Recommendations

- Eliminate the target price program and allocate the target price funding to fixed direct decoupled payments.

- Eliminate rigid loan rates by eliminating the Agriculture Secretary's discretion to freeze loan rates. Use the existing formula in AMTA to set loan rates at 85% of the season average market price for the 5 preceding years excluding the years of highest and lowest prices. Since loan rate formulas are not a perfect answer, Congress should place a 10% cap, up or down, on the yearly adjustment in loan rates. The nominal loan level is not as important as the concept of linking loan rates to market prices. This should eliminate a string of years where loan rates are significantly above market prices. If the Congress feels this change to market adjusted loan rates would reduce grower income too much in the short term, then the Congress should increase the fixed direct payment like the proposal does for oilseeds.

- Eliminate the producer option to adjust payment acres. Base oilseeds payment acres on the most recent three year planted acres with no downward adjustment of payment acres for other crops. This will result in a net increase in total payment acres, but will preserve the "green box " concept of direct payments.

- Hold authorization for the Conservation Reserve Program at 36.4 million acres.

Conclusion

A policy of direct decoupled payments combined with marketing loans which are adjusted annually based on a formula tied to market prices will minimize the distortions in resource allocation caused by farm programs and will:

- Maximize profits from the market place for growers and others in US agriculture.

- Maximize the efficiency of the delivery of farm program benefits to growers.

- Result in higher farm commodity prices over time compared to farm programs with payments coupled to production.

- Maximize the US competitive position in world markets.

CCFAS strongly believes market forces will encourage productivity, good risk management and efficient allocation of resources. Farm programs designed to work together with market forces are the most helpful to farm program participants as well as livestock producers and all the rest of US agriculture. An added bonus is that market oriented policies are not considered trade distorting and therefore are not subject to trade challenges.

CCFAS policy recommendations were developed from information obtained in a study one by WPI/AgriLogic. A copy of the study's report will be provided to the House Agriculture Committee.

Thank you for the opportunity to present the views of the Coalition for a Competitive Food and Agricultural System.